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Accident Insurance

A LECTURE



BY

EDSON S. LOTT

Secretary and General Manager of the United States
Casualty Company
President of the International Association of Accident
Underwriters

DELIVERED AT THE
UNIVERSITY OF PENNSYLVANIA
MAY FOURTH
1905

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ACCIDENT INSURANCE

WHAT IS AN ACCIDENT?

BY the way, *what is an accident?* A clear and comprehensive answer would be warmly welcomed in the claim department of every accident insurance company. Up to date each time some proud discoverer has imagined that his definition would hold—that he has hit upon an unfailing formula—the endless cup-chain of events has dipped down into the bottomless well of evolution and brought to the surface a new and unthought-of combination of circumstances, smashing the formula into little bits. No lexicon comes within hailing distance of a solution.

Suppose, for an instance, a Penn man and a Princeton man should engage in an altercation, and the Princeton man should “break the face” of the Penn man and “put him out of commission.”

Would that be an *accident*?

Perhaps you think it would be an *impossibility*.

Later I shall tell you, briefly, what kind of an accident you must have in order to pry up the lid of an accident insurance company's strong box.

THE BEGINNING OF ACCIDENT INSURANCE IN THIS COUNTRY.

The Travelers Insurance Co., of Hartford, was chartered in 1863, and that may properly be said to be the beginning of accident insurance as it is known to-day. Prior to that English companies had granted insurance against the hazard of railway travel, but general accidents were not considered insurable until then.

The first contract of accident insurance made in this country was for a premium of two cents. Early in the year 1864, while Lin-

coln was still serving his first term as President, James G. Batterson verbally insured James Bolter in the sum of \$5,000 against death if due to an accident occurring while Mr. Bolter walked from the Hartford Post Office to his residence in the same city, the consideration being two cents. At that time The Travelers Insurance Co. was chartered and Mr. Batterson was its president, but it had not begun active business.

That original premium, two one-cent pieces, is still in the possession of The Travelers Insurance Co., and Mr. Batterson, now deceased, became the most famous accident underwriter in the world.

From that small beginning has grown a business of many ramifications and of great importance. About fifteen millions of dollars are now paid annually in this country in personal (or individual) accident insurance premiums alone, while the general business of accident (or casualty) insurance has broadened until it now embraces liability insurance in all its branches, such as the liability (for damages on account of accidental bodily injuries) of manufacturers and contractors to their employes and to the public, the liability of owners of real estate and of owners of horses and automobiles to the public, etc., and also elevator, steam boiler, plate glass, automatic sprinkler, fly-wheel, and other like lines of insurance, while many accident insurance companies now also insure against sickness and burglary.

HOW TO START A STOCK ACCIDENT INSURANCE COMPANY.

There are several kinds of organizations issuing accident insurance in this country to-day—stock companies, fraternal associations, assessment societies and benevolent orders, each operating on a different plan but all organized for the same purpose—the benefit of the organizers.

I shall deal, in my talk with you, with stock companies only.

If any of you intend to organize a stock accident insurance company in the State of New York (whose insurance laws are similar to and illustrative of those of other States, many of which have practically adopted the New York insurance laws), you must first sell at least one hundred thousand dollars of capital stock to *bona fide* cash purchasers, and with the money you must purchase certain securi-

ties and deposit them with the Insurance Department of the State, for the protection of those whom you insure. You can draw the interest on these securities, but you cannot touch the securities themselves so long as you have a policy outstanding or a claim unsettled. They will be held by the State to pay the claims against your company if you cannot pay them out of the premiums you receive, and if you reach a point where the State Insurance Commissioner is of the opinion that you cannot "make good," he will—through the proper legal channel—put your company in the hands of a receiver, who will wind up your affairs, using (in addition to your other assets) as much of your deposit with the State as will be necessary to pay your debts—which will in all probability be all of it.

This one hundred thousand dollars will permit you to write one "line"—say personal (or individual) accident. If you want to write other lines, like steam boiler, plate glass, burglary, etc., then you must increase your capital and sell more stock, and make an additional deposit with the State. A deposit of \$200,000 will permit you to write two lines, while a deposit of \$250,000 will permit you to write all the "casualty" (so called) lines. Most companies write several lines.

Having made the necessary deposit with the State, you are ready for business, except that having deposited every dollar of your capital with the State and not being permitted to withdraw a dollar of it for any purpose whatsoever, you will not have anything with which to pay the expenses of getting your company under way. Beyond all this, the State requires you to keep always on hand (in cash or approved securities) an amount equal to the unearned premiums on all policies you have in force. This is called the reinsurance reserve. The State requires this reinsurance reserve to be maintained unimpaired, that in the event of your assuming greater liabilities than you can carry you will have on hand sufficient premiums with which to pay a solvent company to assume the policies you have issued.

I have stated that the law requires the company to keep always on hand as a reinsurance reserve an amount equal to the sum of the unearned premiums on all the policies it has in force. Accident policies are issued, usually, for one year and the premiums are paid in advance. The premium is "earned" day by day as time goes by and the year rolls around. When the policy has been in force one month,

then one month's premium (or one-twelfth of the year's premium) has been earned and eleven months' premium (or eleven-twelfths of the year's premium) is unearned; when the policy has been in force two months, then two months' premium has been earned and ten months' premium is unearned, and so on. Of course at the end of the eleventh month there has been eleven months' premium earned and there is but one month of unearned premium. As practically all the policies are written for one year, the *average* earned premium is six months, likewise the average unearned premium is six months; hence you will find it necessary to maintain as a reinsurance reserve one-half of your premiums in force at any one time. If at any given time the full premiums on all the policies you have in force amount to one million dollars, then your reinsurance reserve at that time should amount to one-half a million dollars; the average time the policies would have to run being six months. Policies written on a semi-annual and quarterly basis would affect this "easy calculation," but there are not enough semi-annual and quarterly premiums written to warrant further comment.

Having deposited all your capital with the State and being obliged to keep intact as a reinsurance reserve your premiums as fast as they come in, where are you to get the money with which to pay the expenses of organization, the printer, office rent, clerk hire, salaries and traveling expenses of those whom you employ to send through the country to secure agents for your new company, agents' commissions, postage, and the fees and taxes of the various States in which you desire to do business, not forgetting your own salary?

If you are wise, you will have provided for this contingency by having sold your capital stock at a premium. Suppose you capitalize at \$300,000, divided into 3,000 shares, and sell the shares at \$150 each. This will amount to \$450,000,—\$150,000 more than your capital, and this \$150,000 you can use for the purpose of getting under way, leaving your capital and reinsurance reserve unimpaired.

It may be a bit difficult to convince some people that you are offering them a "good thing" when you ask them to pay \$150 for a share in a new company whose par value is but \$100, especially as the newcomer must compete with firmly established and powerful rivals, but the surplus fund you will thus acquire is indispensable. You must have a "working" capital.

THE INTERNAL WORKINGS OF A STOCK ACCIDENT INSURANCE COMPANY.

I suppose I may say a word about the internal organization of a stock accident insurance company, omitting some of the preliminary details necessary to place the company in actual working order.

The active affairs of the company are managed by officers, the president and the secretary or the general manager and the secretary usually being in control with subordinate officers and heads of departments in immediate charge. The officers are elected annually by the directors (sometimes called trustees). The directors are elected by the stockholders, usually for a term of three years. Most boards of directors consist of nine or fifteen or twenty-one members, and their tenure of office is arranged so that one-third retire each year, making it necessary for the stockholders to elect one-third of the full board each year. Under ordinary circumstances, the stockholders meet but once a year and for the sole purpose of electing directors. The directors are commonly vested with the full control of the company and all its belongings. They usually meet monthly to receive reports from and give directions to the officers. Frequently the full board of directors elects from its body a smaller number as an executive committee and this committee keeps in close touch with the affairs of the company and passes upon all but the most important matters.

Then (in theory, at least) the heads of departments report to the subordinate officers, the subordinate officers to the executive officers, the executive officers to the executive committee, the executive committee to the board of directors, and the board of directors to the stockholders, who are the owners of the company.

The executive officers are almost always directors and members of the executive committee, and—as a matter of fact—the executive officers practically control the company and are responsible for its success or failure, and the State insurance departments hold them directly and personally responsible for the proper conduct of the company's affairs. The nature of the business is such that it is absolutely essential to the success of the company that its officers be given the greatest freedom in the exercise of their individual judgment, and it is also of equal importance that the board of directors never relinquish their right to interfere when interference is necessary. For a

board of directors to attempt to handle the details or any considerable part of them, however, would be like the President's cabinet in time of war attempting to direct every movement and every order of a general while engaged in battle. And the successful executive of an insurance company is always engaged in battle—a constant battle for supremacy, which means that the odds are always against him, for he must forever fight against a greater force than his own, every other company being a competitor for the business already on his books as well as for that which he is trying to place on his books.

SUB-DIVISIONS OF DEPARTMENTS.

The general underwriting department of your company will be sub-divided into other departments,—such as the agency (or business producing) department, the accounting department and the claim department.

Of course the most important of these is the agency department, and it should be presided over by a born business producer, one who can place business on your books through his agency corps at a cost which you can afford to pay.

Scarcely less valuable to the company, however, is the claim department, for it is practically the only department which comes in close personal touch with the policyholder, and your success will depend very largely upon the treatment you accord your claimants. Here, as nowhere else, is brought out the complicated and indefinite nature of accident insurance. In most other forms of insurance indemnity is paid under exact and absolute conditions. This is not true of accident insurance. Even in the case of death, it is frequently not at all clear whether death was due to accident or to some other cause. When the claim is for loss of time you must then consider, not only the circumstances in connection with the injury and how it occurred, but also the disability itself—its duration, whether total or partial in itself, whether total or partial in view of the nature of the occupation,—and the trustworthiness of the information concerning these points. Incidentally, too, you must determine the bearing of the claim upon the desirability of continuing the insurance on the risk. The head of your claim department should be selected with infinite care.

You will find that during the policy year one claim will be made for about every seven policies written; that the average period of

total disability will be about three weeks; that during the policy year one out of about every six hundred policyholders will meet death coming within the meaning and intent of your insurance contract—your policy.

POLICY FORMS, AND HOW TO OBTAIN THEM.

When you organize your company you need not, at first, bother much about policy forms, because you can adopt those of leading companies. While new policy features are the fad of the day with accident insurance companies, and while there is a difference in policies, yet—as a rule—one company pays its patrons, in settling claims, about as much as other companies would give under like circumstances, making the result of accident insurance, in this respect, as a whole, about the same to the insured and the insurer irrespective of policy forms and the advertising features in connection therewith. At the same time the trend of the business is to deal with the insured with extreme liberality, and to this may be attributed the increasing popularity of accident insurance.

PURPOSE OF ACCIDENT INSURANCE, PREMIUM CHARGES AND CLASSIFICATION OF RISKS.

When it comes to rates (premiums) and classifications you can also play "follow the leader" (until you become a leader), for while there is a divergence here and there, yet in the main the rates and classifications of the leading companies are the same.

The average accident policy provides the following indemnities: For loss of life, or two feet, or two hands, or one hand and one foot, or two eyes, \$5,000; for loss of one foot, or one hand, \$2,500; for loss of one eye, \$1,666; for total loss of time, \$25 per week—not exceeding 200 consecutive weeks; for partial loss of time, \$10 per week—not exceeding 26 consecutive weeks. The lowest premium for all this is \$20 per year, and the highest premium (outside of a few very dangerous occupations) is \$150 per year.

"Trimminings" of all sorts go with the policy, if the insured wants them or if the agent can make him think he wants them, and for these extras the company charges an additional premium. One of the extras provides that the

insured shall be entitled to double indemnity if he meets with a disabling accidental bodily injury while traveling as a passenger in a conveyance provided by a common carrier. But time prevents discussion of these details.

Speaking of rates, perhaps you thought the two-cent premium paid to Mr. Batterson by Mr. Bolter, in consideration of which Mr. Batterson agreed to pay Mr. Bolter's estate five thousand dollars if Mr. Bolter was accidentally killed while walking from his post office to his residence, was a very small premium. As a matter of fact, it was an enormously high premium. It is estimated that it took Mr. Bolter six minutes to walk the distance. Two cents for six minutes is at the rate of twenty cents for one hour, four dollars and eight cents for one day, \$1,752 for one year. To-day any company in the land would be glad to accept a like risk for one year for ten dollars.

To be entitled to indemnity the insured must suffer a loss caused by bodily injury effected exclusively and directly by external, violent and accidental means which, independently of any and all other causes, immediately and continuously disables him.

The purpose of accident insurance is to reimburse the insured for the financial loss he sustains by reason of an accidental bodily injury of such a nature as to disable him—as to prevent him from attending to the duties of his occupation. Accident insurance does not contemplate pain or inconvenience, *per se*, although many claimants think it should. The policy covers both total disability and partial disability. Total disability (or total loss of time) means that period during which the insured is rendered continuously unable to transact each and every part of his business duties. Partial disability (or partial loss of time) means that period during which the insured is rendered continuously unable to transact one or more of his important and necessary daily business duties.

The policy also insures against loss of sight and loss of limb and loss of life. Indemnity for the loss of time or sight or limb is payable to the insured. Indemnity for the loss of the life of the insured is payable to the beneficiary, whom the insured selects—most frequently his wife.

When one buys accident insurance the premium he pays will depend upon what class he is in, and his classification is determined by the hazard of his occupation. The hazard is ascertained from tables of accidents which have been compiled for many years and by

many companies. In accordance with their relative hazards the various employments of mankind are divided into less than a dozen classes. In some companies these classes are known by descriptive titles, such as special, preferred, extra preferred, ordinary, medium, hazardous, extra hazardous, special hazardous, and so on; while other companies designate them as class one, class two, class three, and so on.

WHAT DETERMINES CLASSIFICATIONS.

It has been stated that the man whose occupation is embraced in the least hazardous class pays \$20 per year for a certain amount of insurance, while a man engaged in an occupation included in the most hazardous class must pay \$150 for the same amount of insurance. From this wide difference in the rate of premium charged different individuals springs the need of accurate classification at the home office of the company. "Familiarity breeds contempt," and the man engaged in a hazardous occupation is the last man to believe that it is hazardous. Of course, in some cases the comparative hazard is apparent; everybody knows that a railroad brakeman is more liable to accidental bodily injury than a college professor—everybody but the brakeman; but everybody does not know that the best of all risks for an accident insurance company is a traveling salesman—if he travels on the cars. He is not so good when he travels by horse and carriage. Suppose we compare the commercial traveler with the dentist, as regards probability of disability from accident. In the first place, taking into account all the losses which have been paid by all the accident insurance companies doing business in this country during the past twenty years, only 4.77 per cent. arose from traveling on the railroad and but 2.74 per cent. resulted from street-car travel, showing that the popular idea regarding the hazard of travel is erroneous. In the second place, a little injury to the dentist's fingers puts him on the retired list for the time being. His fingers must be in normal condition to perform his work. And as he must stand to do his work, a slight injury to his foot is likely to estop him for the time being from following his occupation. But the traveling salesman goes merrily on with one arm in a sling or a crutch in place of one foot, gathering sympathy, admiration and orders as he goes. Indeed, he must go on, unless his jaw-bone is broken or dislocated, for to lay up means big hotel bills and some other fellow

interfering with his "trade." Beyond this, the really good salesman is a man of nerve, not "cheek," but nerve and grit and courage, better remedies than medicine.

These illustrations point to other factors which enter into the classification of an occupation. First among these is what may be termed the *nature* of the occupation. Here we do not consider the effect of the occupation upon exposure to injury, but rather the effect of the injury upon the performance of the duties of the occupation. To illustrate: A barber is not more exposed to accidental bodily injury than a lawyer; the slightest injury to the barber's hands, however, will disable him, while the same injury would merely inconvenience the lawyer and in nowise prevent him from attending to his usual duties. Take the watchmaker; a slight injury to his hand and the deftness and skill, so necessary to his craft, are gone. Let the business manager of a mercantile or manufacturing establishment injure his hand slightly, or even severely, and he goes on his way serenely.

Now consider the nature of the occupation in another aspect—its direct effect upon the injury itself. The surgeon affords an excellent example of this. Think of his constant exposure to septic poisoning in cases of even the most trifling injuries, mere abrasions of the skin. In many other curious ways this nature of the occupation exerts an influence and often explains many of the apparently unfair classifications.

Then there is the "moral hazard," not moral hazard in a general sense, but, specifically, the moral hazard incident to an occupation. It is well known that certain occupations are identified with certain classes, or say "grades," of men. This fact has, of course, a direct bearing upon his moral hazard. This idea also works conversely; that is, occupation has a direct influence upon the morals. Examples of this association between employment and morals are familiar to every one, and I will only refer to instances where the connection is less apparent. It has been found that occupations in which employment is not constant or which, by their character, are not followed during certain periods of the year, are particularly dangerous from the underwriter's standpoint. The actor is frequently unemployed during the summer, certain classes of skilled laborers are idle during certain seasons, the student is idle most of the time, and so on. Experience has corroborated the precepts of the Bible; idleness leads to trouble—for the

accident company. A wound does not heal so quickly, a slight scratch is totally disabling, and sometimes—well, when the insured is out of employment the accident company is supposed to play the role of Lady Bountiful.

There is still another point to consider; the influence of the occupation upon the physical state. Physical condition is, of course, a vital factor in accident insurance; not only is the unhealthy risk more liable to injury and slower and less sure of recovery, but complication by disease is apt to arise, even from a trifling injury. The cause of this influence is often hard to assign, but in many cases it is easily seen. The intemperate habits of certain kinds of laborers, the excessive physical labor required of others, the conditions under which the work is performed, these and many other causes have their bearing.

Absolutely accurate classification can never be attained. The "personal equation," ever prominent in accident insurance, does not permit of this. The lawyer in the country milks his cow and harnesses his horse and does the "chores" about his house, and is thereby more exposed to accident than the city lawyer. The energetic, prosperous lawyer continues at his work even after a severe injury; the less industrious, less prosperous lawyer remains at home to recuperate. Women without steady employment are undesirable accident insurance risks, and men not regularly engaged in an occupation for hire or profit are equally so. Accident insurance is not really insurance against accident, but insurance against loss arising from accident,—loss of life, loss of sight, loss of limb, loss of time,—and only against loss of time when one's time has a cash value. The time of a man of leisure has no money value. Nor has the time of a woman who is not regularly employed. Women book-keepers, clerks and stenographers are good subjects for accident insurance, but teachers and actresses are undesirable because during the summer months they are usually unemployed and at such times a very slight injury is likely to end in a prolonged period of disability. At the same time it may be left for one of you to organize a company to insure only actresses. Perhaps you might recruit your staff of solicitors right here.

While absolutely accurate classification cannot be attained, yet the business of accident insurance is far enough advanced to permit the underwriter to discard theory, and to-day each occupation is rated according to the actual cost of insuring thousands of like risks as shown by

past experience, and when all the occupations insured by any company of considerable size are grouped it is known in advance that the total losses will amount to something less than 50 per cent. of the total premiums received—if the risks are intelligently passed upon at the home office of the company.

MORAL HAZARD.

In addition to occupation and its associated problems there are other features, quite general in their application, that are to be considered in the selection of risks. The applicant must be old enough, and not too old, to be able to take care of himself; his income must, for obvious reasons, exceed the weekly compensation afforded by his policy; he must be temperate in his habits; mentally and physically sound; and he must not live without the pale of civilization.

Then there is the question of moral responsibility. Moral hazard has been mentioned as associated with occupation, but it must also be taken into account in other ways. Immorality—whether due to habitual intemperance or other dissipation, or to financial stress—must necessarily be sufficient reason (when known) for declining a risk. Moral hazard as here used, has, however, a somewhat different meaning. Policies are frequently obtained with intent to defraud. Every company can cite many cases wherein its policyholders have deliberately and carefully (and too often cunningly) planned to rob it—and more or less frequently with success. At times, murder and suicide enter into the scheme, but usually it takes the form of self-mutilation. To the outsider it seems incredible that men will deliberately and permanently cripple themselves that they may secure the benefits provided by their accident policies, but such things have ceased to create wonder in the realm of accident insurance. Men actually do shoot off a hand or a foot or destroy an eye that they may collect indemnity from an accident insurance company.

If you want to test the accuracy of this statement, draw your policy so it will pay \$5,000 for the loss of the right hand and \$1,000 for the loss of the left hand—and you will find that when your policyholder loses a hand, 'tis the right hand which goes. Then change your policy, paying \$5,000 for the loss of the left hand and \$1,000 for the loss of the right hand—and be prepared to discover that your policyholders are losing their left and keeping their right hands. Follow it up and

you will ascertain that often a gun did it (with the aid of the man behind it), and you will frequently ponder over the fact that the "right-handed" man gets his right hand accidentally shot off—when it is \$5,000 to \$1,000 in favor of the right hand—by the accidental (?) discharge of a gun in his left hand; and—strange (?) to relate—the "left-handed" man meets with the loss of his left hand by the discharge (accidental, of course) of a gun in his right hand—when it is \$5,000 to \$1,000 in favor of the left hand. The further you follow this test the more convinced you will be that the moral hazard is the bugaboo of accident insurance. Mutilation by loss of hand is used as an illustration because all accident insurance companies have had to contend with it. Accident insurance companies are defrauded in many other ways. It is often impossible to establish the fraud to the satisfaction of a jury, but it frequently exists just the same.

Then there are the petty cases of fraud—the claimant feigns the injury, he deliberately prolongs the period of disability and demands compensation for something not covered by his policy—and so on. Ofttimes persons of eminent respectability make excessive claims with no thought of wrong-doing. They may charitably be designated as "unconscious malingerers." Some otherwise fair-minded persons persistently pervert the meaning and intent of accident insurance and maintain that their claims should be paid because to turn them down is to assail their integrity. In many cases the agent who secured the risk writes his company that his business will be ruined if the claim is not paid. Some insured and some agents imagine that to whisper the words "man of influence in the community" is sufficient to make the company yield to exorbitant demands, but a well-regulated insurance company cannot afford to recognize class distinctions nor to purchase that uncertain thing—influence. It frequently takes more courage to contest a claim than to pay it, but the company, not only in its own behalf but in behalf of its honest patrons, must refuse to countenance blackmail, even though it suffer, for the time being, by so doing. Every company pays, and it is right that it should pay, claims not coming absolutely within the intent of the policy, but to yield where fraud clearly appears is to violate the trust imposed upon the officers by the company's stockholders and honest patrons.

It must not be thought, from all this talk of fraud, that the percentage of dishonest claims

is large. In fact, the percentage of contested claims is exceedingly small and the overwhelming majority of claimants are honest. At the same time, the dishonest and exorbitant claimant must be reckoned with. It will not do to leave him out of your calculations. He costs time and money.

LOSSES, REINSURANCE RESERVE AND EXPENSES.

Having paid out in losses nearly 50 per cent. of our premiums we are brought back to the reinsurance reserve we were talking about, which—you remember—is an amount equal to the unearned premiums. Altogether this looks like 100 per cent. of the premiums received, and nothing left with which to pay agents' commissions (averaging about 25 per cent. of the premiums), the printers' bills (a large item with insurance companies), postage (another big item), office rent, clerk hire (another important item, as the entire business is one of detail record), salaries and expenses of traveling representatives (and no company can do business without them), State fees and taxes (the latter amounting to 3 per cent. of the gross premiums in some instances), the salaries and expenses of the insurance department examiners (which must be paid by the company), officers' salaries (and if you want competent officers you must pay liberal salaries), directors' fees (a considerable item in the course of a year), and stockholders' dividends (the very thing you promised when you sold your stock).

How can you do it?

Well, at first you can't, and that is why you sold your stock at \$150 per share, instead of \$100—the par value. However, if your officers have a technical knowledge of the business; and if—in addition—they work early, late and all the time; if they possess enthusiasm themselves and the ability to impart it to all others connected with the company, including the agency staff as well as the home office force; if they can unerringly separate the fraudulent from the honest claimants; if they can pay a just claim in a manner calculated to make the policyholder feel that the company was organized for that very purpose, and have the courage to let the fraud appeal to the courts; if they know how to cause every employee and every patron to realize that all he is entitled to is a "square deal"; if they have the mental and physical endurance necessary to untie hard knots and disentangle difficult problems every day of their lives; if they are constantly posted

on the ever-changing insurance laws of each State in which the company does business; if they are original and bold and conservative, all at the same time; if they are tactful and tireless,—then there is a way whereby they can make a profit for the owners of your company. Indeed, some men succeed in the business who are not the ideal described; they are those who have a fair amount of these attributes and make up the balance by sheer hard work, by keeping everlastingly at it; and keeping everlastingly at it almost always brings success in any field of human endeavor.

After all this preamble, it may be stated that if your premiums the first year amount to say \$500,000, and your policies are all on an annual basis, and the average time they have to run at the end of the year is six months, and consequently you have set aside as a reinsurance reserve \$250,000, and the next year your premiums amount to \$600,000, then you need only put up an additional \$50,000, for at that time your premiums actually in force will be but \$300,000. In other words, after having set aside any amount for a reinsurance reserve you need not increase that amount except as your business increases; hence, if you do the same amount of business the second year as you did the first year, you need not set aside any more reserve,—you can use your entire premium income with which to pay losses and expenses, and your losses should not reach quite 50 per cent. of the premiums.

INVESTMENT EARNINGS.

Another very important item has not been mentioned. It is the item of investment earnings. The capital of an insurance company is invested in interest-bearing securities. So is the reinsurance reserve. Likewise the surplus, if there is any, and every well regulated company has a surplus. The amount set aside for claims in the process of adjustment is drawing interest, too. These items go to make up the company's assets, and as the business grows these items grow, until the original capital is but a small part of the total holdings of the company.

Suppose the original capital of \$300,000 is intelligently nursed until the total assets are \$2,000,000, and the entire amount is safely invested in securities which average a net income of $4\frac{1}{2}$ per cent. This means \$90,000 a year from this one source, or 30 per cent. per annum on the capital stock. In that event you can pay out, in losses and expenses, 100 cents

for every dollar of premium you receive and still make your stockholders happy—and, in time, opulent. And then, you need not stop with assets of \$2,000,000; you can go on and on, and grow and grow, and your dividends can also go on forever.

IMPORTANCE OF INTELLIGENT INVESTMENTS.

It appears, then, that there are two principal departments in an insurance company, the insurance (or underwriting) department and the banking (or investment) department, and while the underwriting department must first furnish the funds for the banking department to invest, the success of the company will largely depend upon the intelligence exercised in these investments. The securities must be safe, and at the same time profitable, for an additional one-half of one per cent. on \$2,000,000 is \$10,000 per year, 3 1-3 per cent. on a capital of \$300,000; and when your total holdings amount to \$10,000,000—but that may be too far ahead to talk about now.

Should you reach a point where your interest amounts to \$90,000 per year it would be most unwise to pay it all out in dividends to your stockholders; you should create a surplus,—for a bad year, for an epidemic of losses, to show your patrons that you could stand reverses and still pay your claims. Indeed, should you have no surplus you would be in constant danger of going into the hands of a receiver. Any day may bring you a loss of many thousands of dollars, and the following day may be worse. Whenever you reach a point where you have no surplus, where your assets equal your liabilities and no more, then you are right up to the dead line, and should a loss force you over the line, you will soon find the receiver in possession.

SUPERVISION AND EXAMINATION BY THE STATE.

Each State has an insurance department presided over by an officer usually known as the Insurance Commissioner, and this official practically has supreme authority over the insurance companies doing business in his State, so far as the business they do in his State is concerned, whether the companies were chartered by his State or by another State. The charter you receive from the State where you organize does not (of itself) permit

you to do business in any other State. Before doing business in any other State you must obtain a license from the Insurance Commissioner thereof, and this may or may not be an easy task.

The affairs of your company will be constantly scrutinized by the insurance department of your own State as well as by the insurance department of every other State where you are permitted to do business, and you will be periodically examined by your own insurance department and more or less frequently examined by the insurance department of other States. Sometimes the examiners sent by the insurance departments will be insurance experts and sometimes they will be political sharks, but each will come clothed with full power to go through everything in sight. It has been said that in days gone by there was mighty little in sight after certain Western examiners left the company they had "examined."

SURPLUS AND ASSETS.

Surplus is, as you know, the difference between your liabilities and your assets. Your liabilities are made up from your reinsurance reserve, the amount you owe for claims (losses), and all your other indebtedness (the amount you owe the landlord, the printer, etc.). Your assets are, of course, your belongings, your holdings—whatever you are "worth" before paying your debts.

SOME CURIOUS CLAIMS.

Let me tell you about some curious claims.

A Vermonter wrote: "The doctor ordered a Spanish fly blister for my wife. It was laid on the dresser. When she wanted it, it could not be found. Several times that day I thought my new shoes were chafing my ankle. Upon removing my shoes that night we found the missing blister, and I missed about two inches of skin at the same time. Have not been able to attend to my duties since."

One policyholder swallowed a gold tooth and drew five weeks' indemnity.

Another patron lacerated his thumb "while cutting coupons."

Another was "bitten by a lobster," so he wrote the company.

A Washington man wrote: "On the morning in question, on entering the kitchen, my wife, who had been using a flat-iron, told me

to let her remove a crease in my pants, saying at the time that the iron was not hot. I placed my leg in position on a chair, she placed a damp cloth over the place or crease and put the iron over this. The iron, being hotter than either of us supposed, drove the steam, thus generated, through the pants to the flesh, thus steaming the place the full length and nearly the width of the face of the iron, about two inches by six inches, on my leg from the knee-cap upwards."

A man struck a match at the desk of a hotel and the head of the match flew off and landed in the ear of the hotel clerk, totally disabling him for twenty-seven days.

A Pittsburg policyholder placed an electric fan beside his bed on a hot night, and while asleep stuck his foot into the fan, waking up minus a big toe.

A young man working in a saw mill lost his finger "monkeying with the buzz saw." When he recovered he went back to work and promptly lost another finger "showing a friend how he lost the first one."



